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IN THE

Supreme Court of the United States

EBAY INC. AND HALF.COM, INC.,
Petitioners,

v.

MERCEXCHANGE, L.L.C.,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

BRIEF OF TIME WARNER INC., AMAZON.COM, INC., CHEVRON CORP., CISCO SYSTEMS, INC., GOOGLE INC., IAC/INTERACTIVE CORP., INFINEON TECHNOLOGIES AG, SHELL OIL COMPANY, VISA U.S.A., INC., AND XEROX CORPORATION AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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INTERESTS OF *AMICI CURIAE*[1]

Amici are major corporations that are leading providers of goods and services in high technology industries. *Amici* own thousands of valuable patents that are integral to their businesses. They manufacture and distribute goods and services that contain numerous subsidiary components that are patented and employ many processes that are patented.

As holders and licensees of valuable patents, *amici* are keenly aware of the need for effective remedies against infringement, and they strongly support the availability of injunctive relief in appropriate cases. At the same time, however, *amici* are also frequently the subject of patent suits, including many suits that make abusive use of the patent system to extract lucrative settlements that are disproportionate to the value of the litigated patent. *Amici* therefore have a strong interest in ensuring that the remedial rules governing patent cases are fair to both plaintiffs and defendants.

Amicus Time Warner Inc. is a leading global media and entertainment company with businesses in filmed entertainment, interactive services, television networks, cable systems and publishing media, including America Online, Time Inc., Time Warner Cable, Home Box Office, New Line Cinema, Turner Broadcasting System and Warner Bros. Entertainment. A frequent innovator on the forefront of technology, Time Warner has pioneered such industry-shifting products as the DVD and digital cable. It holds numerous patents relating to its products and services.

Amicus Amazon.com, Inc. is one of the world's largest and best known online retailers. It operates websites where, along

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[1] Counsel for all parties have consented to the filing of this brief, and their consents have been filed with the Clerk of this Court. No counsel for either party had any role in authoring this brief, and no person other than the named *amici* and their counsel has made any monetary contribution to the preparation and submission of this brief.

with other retailers, it offers millions of unique, new, refurbished and used items in a broad array of categories. In providing this innovative service, Amazon.com employs many patented technologies.

Amicus Chevron Corporation is a leader in the energy industry. Chevron explores for and produces oil and natural gas, including complex deep water exploration and production in the Gulf of Mexico and around the world. Chevron also transports natural gas in the United States through pipeline systems and liquefied natural gas around the world in special tankers; refines oil into fuels, lubricants, and base chemicals; and develops several advanced energy technologies such as fuel cells, hydrogen storage and gas-to-liquid products. These activities involve numerous complex process that are the subject of patents, and the products Chevron sells frequently contain patented components such as additive packages.

Amicus Cisco Systems, Inc. is a recognized leader in Internet technology. It sells software, hardware such as routers and switches, and services that together provide fast, durable, and secure networks over the Internet for business, education, government, and home communications. These products incorporate many patented components and processes.

Amicus Google Inc. is a global technology leader whose mission is to organize information and make it universally accessible. Google maintains one of the world's largest online indices of websites and other content. Its automated search technology helps people obtain nearly instant access to relevant information from its vast online index, and its AdWords program provides targeted, online advertising for the products and services of its partners. In providing these products and services, Google uses many patented technologies.

Amicus IAC/InterActiveCorp is a diversified e-commerce company whose businesses are leaders in numerous sectors of the Internet economy. IAC's operating businesses include Ask Jeeves, Citysearch, Entertainment Publications, Evite,

Gifts.com, HSN, Interval International, LendingTree, Match.com, ServiceMagic, and Ticketmaster. Due to their high visibility, IAC and its businesses receive frequent licensing demands and litigation threats from holders of patents of questionable technological value, most of whom do not practice their patents.

Amicus Infineon Technologies AG is a leading innovator in the semiconductor industry with locations throughout the United States, Europe, and Asia. It designs, develops, manufactures, and markets a broad range of semiconductors and complete system solutions for a wide range of industries. Its products, used in virtually every application from cell phones to supercomputers, are integral for wireless and wireline communications, automotive, industrial, computer, and security and chip card markets. Its innovative technologies and products are covered by thousands of patented components and processes.

Amicus Shell Oil Company is a leader in the energy industry. It engages in exploration, production, refinement, and transportation activities throughout the world. In addition, Shell develops and employs technologies relating to wind energy generation, solar photovoltaic, and other alternative energy sources such as coal gasification, biofuels, geothermal, and hydrogen. These activities frequently involve complex processes that are the subject of numerous patents, and the products it manufactures and sells frequently contain patented components.

Amicus Visa U.S.A., Inc. is part of a worldwide association of more than 21,000 financial institutions offering Visa-brand payment services, including Visa-brand credit cards. These services include an extensive system for approving and processing charges involving millions of merchants and cardholders as well as thousands of banks daily. Multiple components of this system, including a range of business methods and technological features, consist of or contain patented elements.

Amicus Xerox Corporation is a technology and services enterprise that helps businesses deploy Smarter Document Management[SM] strategies and better ways to work. Xerox offers an array of innovative document solutions, services and systems including digital presses, printers, multifunction devices and associated supplies, software and support. Xerox holds thousands of patents relating to the hardware, software, and services it offers.

SUMMARY OF ARGUMENT

The Federal Circuit's rule that injunctions should issue virtually automatically in patent infringement actions is wrong as a matter of statutory construction and historic principles of equity. It also has grave practical consequences for the operation of high-technology companies. By effectively eliminating equitable discretion over injunctive relief, the Federal Circuit's rule invites or requires injunctions that impose costs on manufacturers that are wholly unrelated to the value of the patent infringed, and as a result give patentees the leverage to extract vast windfalls. Under such circumstances, injunctions do not serve the goal of the patent system to promote innovation but turn that system on its head.

The automatic injunction rule can lead to grossly inequitable results affecting technology-dependent businesses. First, it can do so when an infringement claim concerns a minor element of a complex good or service. Where a minor but nonetheless infringing component is embedded in a complex process in which a firm has invested significant fixed capital, an injunction can force the manufacturer to shut down or retool the entire process, incurring enormous expense. In such circumstances, the threat of an automatic injunction enables patent litigants to leverage patents that themselves have low value into disproportionately valuable settlements.

Second, the availability of automatic injunctive relief can enable holders of dubious patents to use them to extract

lucrative license fees through threats of litigation. Holders of patents having little technical merit may nonetheless assert broad claims that significantly overlap a manufacturer's operations. Because patent infringement is easy to assert, while patent invalidity is difficult to prove, and patent litigation is very expensive, the threat of a virtually automatic injunction can induce a patent defendant to pay high fees for a license even where the patent would likely be invalidated if protracted litigation were endured.

Third, both these sorts of windfalls from the automatic injunction rule have encouraged the rise of a new class of professional patent litigants that operate as holding companies for patent portfolios rather than inventors or practitioners. The automatic injunction rule encourages these non-practicing entities to seek disproportionate returns on their patents through litigation or the threat of litigation. Such litigation further burdens a court system already overstretched by the rise in patent litigation.

Finally, automatic patent injunction can impose significant burdens on consumers and the public interest that are not covered by the Federal Circuit's narrow exception for extraordinary and imminent harm to public health. They include, for example, the loss of access to medically needed procedures or vital communication networks.

The automatic injunction rule not only imposes costs on producers and the public, but also distorts the patent system and undermines the goal of innovation that it is meant to serve. The goal of the patent system is "[t]o promote the Progress of . . . useful Arts." U.S. CONST. art. I, § 8, cl. 8. But the rule encourages opportunistic litigation that diverts resources that could be used to develop innovative new products and processes, and distorts the focus of the research that does take place. The automatic injunction rule also encourages abusive practices at the Patent Office, such that

patent applicants spend more time inventing patents than patenting inventions.

These costs to technology producers are unnecessary, as patent law provides patent holders with other powerful remedies. The Federal Circuit's unique rule for patent injunctions therefore should be overturned and patent law should return to the traditional, flexible approach to injunctive relief employed in other areas of federal law. Under traditional balancing of the equities, district courts that are closest to the facts could take into account such factors as the burden that an injunction would impose upon a defendant to break up fixed capital investment, the defendant's ignorance of a patent while making such investments, the technical value of the patented product or process, the plaintiff's actual practice or licensing of the patent at issue, and the plaintiff's conduct at the Patent Office and after issuance. Injunctive relief could still issue under such a flexible approach where appropriate on traditional grounds.

ARGUMENT

In the decision below, the Federal Circuit held that the plaintiff was "entitled," and had a "right," to a permanent injunction, *MercExchange, L.L.C. v. eBay, Inc.*, 401 F.3d 1323, 1339 (Fed. Cir. 2005), even though the district court, which was closest to the facts, had denied such an injunction based upon weighing the equities in the case. The Federal Circuit thus foreclosed, for patent infringement cases, the application of well-established principles of equity over which trial courts have discretion in all other areas of federal law. *See, e.g.*, *Weinberger v. Romero-Barcelo*, 456 U.S. 305, 312 (1982) (noting that the propriety of injunctive relief depends upon (i) whether the plaintiff will suffer irreparable injury, (ii) whether the plaintiff has an adequate legal remedy, (iii) whether the injunction serves the public interest, and (iv) whether the balance of hardships tips in favor of the plaintiff).

Instead, the Federal Circuit has required that injunctions issue virtually automatically upon a finding of patent infringement.

This unique and inflexible approach conflicts with the plain text of the Patent Act, which provides that district courts "*may*" grant injunctive relief "in accordance with the principles of equity" and "on such terms as they deem reasonable." 35 U.S.C. § 283 (emphasis added). It is also at odds with prior tradition by which the federal courts had interpreted this statutory language to confer the same equitable discretion in patent cases that is enjoyed in other types of cases. *See, e.g., Foster v. Am. Mach. & Foundry Co.*, 492 F.2d 1317, 1324 (2d Cir. 1974) ("An injunction to protect a patent against infringement, like any other injunction, is an equitable remedy to be determined by the circumstances. It is not intended as a club to be wielded by a patentee to enhance his negotiating stance." (citation omitted)).[2] Nothing in the purposes or practical realities of patent law requires the Federal Circuit's rigid rule.

I. THE AUTOMATIC INJUNCTION RULE GRANTS PATENT HOLDERS LEVERAGE TO EXTRACT UNJUST WINDFALLS

Patent injunctions are potent remedies. They can force a defendant to shut down a production line or withdraw a product from the market altogether, with potentially grave results. *See* ADAM B. JAFFE & JOSH LERNER, INNOVATION

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[2] Although the Federal Circuit initially appeared to recognize the district courts' statutory and traditional discretion in patent infringement actions, *see Roche Prods., Inc. v. Bolar Pharm. Co.*, 733 F.2d 858, 865 (Fed. Cir. 1984), *superseded on other grounds by statute*, 35 U.S.C. § 271(e), *as recognized in W.L. Gore & Assocs. v. C.R. Bard, Inc.*, 977 F.2d 558, 560 (Fed. Cir. 1992), that court has since granted permanent injunctions increasingly reflexively, even though it inconsistently still balances the equities for preliminary injunctions. *See* HERBERT F. SCHWARTZ, PATENT LAW AND PRACTICE 193-97 (4th ed. 2003).

AND ITS DISCONTENTS 113-14 (2004) (noting that one patent injunction cost Kodak $200 million in losses and 4,500 lost jobs). A firm that tries to design around an injunction and fails will find itself in contempt proceedings. The threat of such an automatic remedy can become a powerful club in the hands of some patent litigants, enabling them to extract license fees disproportionate to the value of the patent, and to impose significant additional social costs.

A. The Automatic Injunction Rule Allows Patent Litigants To Extract Disproportionately Valuable Settlements In Cases Involving Complex Products And Services

The Federal Circuit's automatic injunction rule provides no exception for injunctions that would effectively prevent the use of an entire complex product line or service when the patent in question covers only a minor element of that product or service. In such cases, the decision below compels courts to issue grossly inequitable injunctions that allow patent litigants to leverage narrow patents into returns far exceeding their intrinsic value.

Today's complex goods and services contain numerous hardware and software components. Some of these components are central to those products, while others serve only minor functions that could be served by other products or processes. As patents increase exponentially in number,[3] many of the components needed to produce a single product—even minor components—are potentially subject to patent infringement claims. "In some industries, such as computer hardware

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[3] In the last two decades, the number of patent applications filed with the United States Patent and Trademark Office ("USPTO") has more than tripled, from 125,931 to 409,532, and the number of patents issued has doubled, from 77,400 to 157,900. *See* USPTO, PERFORMANCE AND ACCOUNTABILITY REPORT, FISCAL YEAR 2005, at Table 2 (2005), http://www.uspto.gov/web/offices/com/annual/2005/060402_table2.html.

and software, firms can require access to dozens, hundreds, or even thousands of patents to produce just one commercial product." FEDERAL TRADE COMMISSION, TO PROMOTE INNOVATION: THE PROPER BALANCE OF COMPETITION AND PATENT LAW AND POLICY 6 (2003) ("FTC REPORT"), http://www.ftc.gov/os/2003/10/innovationrpt.pdf. In nearly all industries and especially in the high technology field, a manufacturer thus must navigate through an ever denser "thicket" of patents to ensure that the many components it employs to make a single product are noninfringing.[4]

If a manufacturer is aware of such a patent in advance, it can often avoid any infringement claim by negotiating a reasonable license, designing around the patent, or replacing it using a noninfringing alternative. For this reason, patents covering minor elements of a product or service often have little or no value in themselves. *See, e.g.*, WILLIAM M. LANDES & RICHARD A. POSNER, THE ECONOMIC STRUCTURE OF INTELLECTUAL PROPERTY LAW 320 n.52 (2003) (noting that over 95% of patents are unlicensed and 97% generate no royalties).

But the sheer number of patents and complexity of manufacturing processes often prevent such advance knowledge of potential patent infringement by a minor component. Technology producers invest enormous fixed capital in complex manufacturing processes and software programs. Even where it would have been relatively easy to design around a patented element in advance, doing so once huge fixed costs have been incurred is not. To the contrary, it can be enormously expen-

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[4] Carl Shapiro, *Navigating the Patent Thicket: Cross Licenses, Patent Pools, and Standard-Setting*, *in* 1 INNOVATION POLICY AND THE ECONOMY 119, 119-22 (Adam Jaffe *et al.* eds., 2001). *See also* FTC REPORT at 31 (noting that the "growth of the knowledge-based economy presents several challenges to the patent system . . . [including] the sheer number of patents sought and received").

sive to incorporate a new noninfringing minor element into a larger manufacturing process or software program.[5]

Most manufacturing processes now use process-control systems based on information technology. These systems contain small controllers and other components that are manufactured for incorporation into larger process-control systems. While such components have relatively little market value, the systems into which they are integrated are so intertwined with manufacturing processes that their removal can shut down the entire manufacturing process.

Even if a new minor component can be integrated into a complex product or service, launching and testing it can be very expensive. For example, a change in semiconductor manufacturing equipment, even if small, might require re-qualification of the equipment by most or all of the customers using that equipment, which can take months of work by each customer to make sure the change does not affect the quality of the customer's final product. Many other manufacturers, particularly regulated manufacturers like medical device companies, face similar difficulties.

Similarly, a new software subroutine cannot simply be substituted for an older infringing one. The different subroutines in large software programs frequently have unexpected interactions with each other, and it is therefore necessary to spend considerable time "debugging" software programs before releasing them to the public.[6] And because

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[5] *See, e.g.*, Rosemarie Ziedonis, *Patent Litigation in the U.S. Semiconductor Industry*, *in* PATENTS IN THE KNOWLEDGE-BASED ECONOMY 191 (Wesley M. Cohen & Stephen A. Merrill eds., 2004) (noting that a facility for producing computer chips can cost more than $1 billion).

[6] *See, e.g.*, James Bessen, *Open Source Software: Free Provision of Complex Public Goods*, RESEARCH ON INNOVATION, at 5 (2005), http://www.researchoninnovation.org/opensrc.pdf (noting that most of the cost of software "arises from testing, debugging and consumer maintenance (that is, fixing bugs or providing work-arounds after product release)").

software is frequently distributed to many client applications, changing it is more challenging than swapping one hardware module for another.

The delay associated with incorporating a new element into an existing product can also be costly. During the time it takes to install new equipment on a production line or debug new software, a manufacturer might lose significant sales to its competitors. It might also be forced to recall and replace products used by its consumers, incurring additional costs to its reputation and good will if customers blame the disruption on the manufacturer. *See* Samson Vermont, *The Economics of Patent Litigation*, *in* FROM IDEAS TO ASSETS: INVESTING WISELY IN INTELLECTUAL PROPERTY 350 (B. Berman ed., 2002).

Given the practical realities of today's technology-dependent operations, it is easy to see why the automatic injunction rule enables patent litigants to hold up technology companies in infringement cases for settlements far exceeding the intrinsic value of a patent. An injunction against use of a minor patented feature embedded in a complex manufacturing process or software program not only will stop use of that element, but also will trigger the heavy additional costs of retooling, retesting and delay described above. For most companies that have invested fixed capital in design, development or manufacturing, the risk of an injunction against even a minor component of its production is "unacceptable." Steven Z. Szczepanski, *Licensing or Settlement: Deferring the Fight to Another Day*, 15 AIPLA Q. J. 298, 301 (1987).

For example, a patent holding company that does not make a product obtained a recent injunction against Research In Motion, Ltd., the maker of the popular wireless BlackBerry product and services. *NTP, Inc. v. Research In Motion, Ltd.*, 418 F.3d 1282, 1287 (Fed. Cir. 2005), *cert. denied* 74 USLW 3371 (U.S. Jan. 23 2006) (No. 05-763). Although the injunction shutting down RIM's BlackBerry service was stayed

pending appeal, the Federal Circuit ultimately upheld the district court's ruling. *Id.* In December 2005, RIM faced the prospect of a shutdown of its network and services as a result of the injunction. Ian Austen, *Bye Bye BlackBerry? A Patent Dispute Threatens To Cut Executives Off*, N.Y. TIMES, Dec. 3, 2005, at C1. While in theory RIM might have designed around the infringed patent claims, in practice RIM was unable to do so because of the risk and expense of altering an aspect of a complex network. *Id.*

To avoid the issuance of such an injunction, a rational manufacturer might well settle with the patent holder, taking a license for a fee that is less than the cost imposed by the injunction but more than the fair value of the patent.[7]

B. The Automatic Injunction Rule Enables Patent Holders To Reap Lucrative License Fees From Patents Of Dubious Technical Merit

Automatic injunctions increase the leverage patent holders can exert not only where narrow patents are asserted against elements of complex products, but also in cases of broad, vague patents of dubious technical merit. Patent law seeks to "stimulate the efforts of genius" by "holding out a reasonable reward to inventors, and giving them an exclusive right to their inventions for a limited period." *Pennock v. Dialogue*, 27 U.S. 1, 19 (1829) (Story, J.). To encourage inventors to incur "enormous costs in terms of time, research, and development," *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470 (1974), they "must expect that once commercialization occurs, product prices can be held above postinvention production and marketing costs" long enough for them to recoup the costs of their the front-end investments. F.M. SCHERER &

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[7] *See, e.g.*, Michael J. Meurer, *Controlling Opportunistic and Anti-Competitive Intellectual Property Litigation*, 44 B.C. L. REV. 509, 512-20 (2003); JAFFE & LERNER, *supra*, at 111; Ziedonis, *supra*, at 191.

DAVID ROSS, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE 622 (3d ed. 1990).

These policies are not served by technically questionable patents that teach little to those skilled in the art. But the automatic injunction rule creates opportunities for even scientifically marginal patents to receive supracompetitive returns. When such patents are asserted against capital-intensive technology-dependent industries and backed by the threat of an automatic injunction, they take on economic value out of proportion to their technical merit. "Considering that a bad patent verdict could cripple or destroy a company, many target companies make the difficult but practical decision to take a license, even when the asserted patent is suspect." Jeremiah Chan & Matthew Fawcett, *Footsteps of the Patent Troll*, 10 INTELL. PROP. L. BULL. 1, 4 (2005).

The classic practitioner of such sharp dealing with dubious patents was the late Jerome Lemelson, a prolific procurer of patents and frequent patent litigant. By 2004, Lemelson's foundation was the owner of approximately 185 unexpired patents and many pending patent applications. *See Symbol Techs., Inc. v. Lemelson Med., Educ. & Research Found., L.P.*, 422 F.3d 1378, 1380 (Fed. Cir. 2005). Lemelson alleged that some of those patents covered the use of bar codes on commercial products. Rather than suing companies that market and manufacture bar-code readers, Lemelson sued companies that simply used these machines, typically settling for an amount just under the expected cost of litigation. *See* Nicholas Varchaver, *The Patent King*, FORTUNE, May 14, 2001, at 214-16. In this way, he earned hundreds of millions of dollars in licensing fees. *See id.*; *see also* Stewart Yerton, *The Sky's the Limit*, THE AMERICAN LAWYER, May 1993, at 64.

The Lemelson bar code patents arose from applications filed in 1954 and 1956. *Symbol*, 422 F.3d at 1380. Thus, Lemelson asserted in the marketplace a patent monopoly *fifty*

years after the alleged inventions. Eventually, the manufacturers of bar code scanners filed a declaratory judgment action and forced a trial to determine validity, resulting in a decision that the patents were invalid, not infringed and unenforceable. *See Symbol Techs., Inc. v. Lemelson Med., Educ., & Research Found., L.P.*, 301 F. Supp. 2d 1147 (D. Nev. 2004), *aff'd*, 422 F.3d 1378 (Fed. Cir. 2005). With respect to validity, the trial court found that the patent claims were not enabled because the technical disclosure in the Lemelson patents did not teach one of ordinary skill in the art how to build and use a bar code scanning system. *Id.* at 1165-66. But for years before this trial, aided by the leverage of the automatic injunction rule, Lemelson was able to reap hundreds of millions of dollars in royalties.

The leverage exercised by Lemelson reflects unique structural aspects of the patent process that drive up the actual and threatened cost of patent injunctions. Unlike traditional property rights, patent rights are defined by the patentee. Real property consists of a plot of land with fixed metes and bounds defined by deed. The value of personal property is determined by how much a buyer is willing to pay in the market for a physically definite object. Copyright attaches once original content is fixed in tangible form; copyright law protects but does not define that content. *See* 17 U.S.C § 102.

In contrast, patentees themselves, together with the examiners in the Patent and Trademark Office, define the scope of the property protected by patent law. Patent coverage is defined by the "claims" set forth by the patentee. 35 U.S.C. § 112. Each patent contains many claims of varying scope. *See* ROBERT C. FABER, LANDIS ON MECHANICS OF PATENT CLAIM DRAFTING 191-93 (1990). Each claim is a separate invention, and each claim is considered independently valid.

35 U.S.C. § 282. Patent applicants have strong incentives to draft claims broadly.[8]

Not only do patent applicants create the scope of their own property, but they do so *ex parte* at the Patent Office. *See* SCHWARTZ, *supra*, at 30. This means that those who may be affected by the scope of the patent right—the public and potential infringers—have little or no say about the rights being granted until the patent issues. *Id.*; *see also* Chan & Fawcett, *supra*, at 10 (noting that third-party reexamination procedures are generally ineffective). There is no need to actually build a working model or do any technical work to apply for a patent. The applicant need only convince the Patent Office that the technical disclosure would teach those of skill in the art to build the claimed invention. The exponential increase in patent applications often causes overworked patent examiners to rely on patentees to explain technologies. And unlike in trademark law, the patentee has no later obligation to convince the Patent Office that it engages in continued use.

Once a patent issues, it is presumed to be valid. 35 U.S.C. § 282. This presumption has important practical consequences. While infringement is easy to assert, invalidity is difficult to prove. Accused infringers must overcome the high evidentiary burden of proving "clear and convincing" evidence that a patent is invalid. *Oakley, Inc. v. Sunglass Hut Int'l*, 316 F.3d 1331, 1339 (Fed. Cir. 2003). In addition, patent infringement and validity both raise fact questions for the jury, usually involving expert testimony. As a result, dismissal on the pleadings is not available, and summary judgment motions can usually only occur after fact and expert discovery have closed and the trial judge has conducted a

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[8] Indeed, patent attorneys have a professional responsibility to seek the broadest possible claims for their clients. *See Solomon v. Kimberly-Clark Corp.*, 216 F.3d 1372, 1382 (Fed. Cir. 2000).

Markman hearing to construe the claims—subject to *de novo* review by the Federal Circuit.

In light of the complexity of claim construction, the heavy reliance upon expert testimony, the difficulty juries have assessing evidence of infringement, and *de novo* appellate review of claim construction, patent defendants can rarely be entirely sure of victory, irrespective of the strength of an invalidity defense. Patent litigation is also extremely expensive. The "industry rule of thumb" is that "any patent infringement lawsuit will easily cost $1.5 million in legal fees alone to defend," and for patent suits involving damage claims of more than $25 million, expenses can increase to $4 million per side.[9]

In addition to all these reasons not to challenge the validity of dubious patents, a successful validity defense gives a free ride to a defendant's competitors. Under *Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation*, 402 U.S. 313 (1971), if a patent is found invalid in an earlier lawsuit, an alleged infringer can rely on this judgment for issue preclusion in a later suit. Thus, any patent defendant has reduced incentive to fight for a judgment of patent invalidity, because a favorable ruling would benefit the defendant's competitors at no cost to them. *See* Joseph Scott Miller, *Building A Better Bounty: Litigation-Stage Rewards For Defeating Patents*, 19 BERKELEY TECH. L. J. 667, 668-69 (2004).

The automatic injunction rule compounds the risk of losing an infringement case under these conditions of high litigation cost, outcome uncertainty, and structural asymmetries that favor the patent holder and discourage the litigation of patent validity. It thus allows even broad, vague patents of dubious

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[9] WENDY H. SCHACHT & JOHN R. THOMAS, PATENT REFORM: INNOVATION ISSUES 7 (2005) (internal citations omitted); *see also* JAFFE & LERNER, *supra*, at 14 (noting the indirect costs of patent litigation).

technical merit to be used as leverage to extract lucrative license fees.[10]

C. The Automatic Injunction Rule Encourages The Rise Of Non-Practicing Patent Litigants

Well aware of the above dynamics, a new class of professional patent litigants has appeared in recent years. *See* SCHACHT & THOMAS, *supra*, at 9 & n.12 (noting that such entities are often called "patent trolls"). These litigants do not practice their patents, seek to develop new products based on their patents, or enter into licenses with companies that want to develop the innovations covered by those patents. Instead, they seek out companies that have independently developed similar innovations and then either sue them or extort licenses out of them based upon the threat of suit.

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[10] Other examples of broad, vague patents that can benefit disproportionately from the automatic injunction rule are those related to industry standards. In many technology fields such as networking, telecommunications and computer manufacturing, various components and equipment must be able to interconnect with each other and have compatible software. The Internet depends upon such interoperability. Accordingly, the public good is well served by organizations through which technology producers cooperate to set interoperability standards. Patent holders, however, can craft patent claims that specifically cover such standards. Once a particular industry has agreed to adopt the standard, the capital invested is significant, and the threat of injunction, immense. Many standards organizations therefore condition membership on agreeing to disclose pending patent applications and license intellectual property that covers the standard on fair and reasonable terms. *See* Mark A. Lemley, *Intellectual Property Rights and Standard-Setting Organizations*, 90 CAL. L. REV. 1889, 1904 (2002); Janice M. Mueller, *Patent Misuse Through the Capture of Industry Standards*, 17 BERKELEY TECH. L.J. 623, 635-36 (2002). For the patent holder who is not a manufacturer and not a member of the organization, however, there are no such counterbalancing forces, and the automatic injunction threat becomes a potent weapon. Thus, even an innocent adopter of an existing interoperability standard based on technology developed by reputable vendors can face liability as a patent litigant selects its targets.

Some such repeat patent litigants focus upon buying dormant, unexploited patents.[11] For example, the Acacia Technologies Group, which controls more than 140 patents, describes itself as a company that "develops, acquires, and licenses patented technologies"; it employs more lawyers and accountants than engineers, and its engineers reportedly evaluate rather than develop technologies.[12] Other frequent patent litigants are failed market participants who turn to litigation after unsuccessfully attempting to commercialize technologies allegedly related to their patents.[13]

The automatic injunction rule gives such sophisticated professional patent litigants additional leverage to extract unjust settlements and license fees. The non-practicing patent plaintiff has no capital investments or technology of its own at stake. A company's own patent portfolio is "a shield or bargaining chip in a traditional IP dispute" between competitors, but is of little value against a plaintiff that does not practice its patent or make products. Chan & Fawcett, *supra*,

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[11] *See* Stephen A. Merrill *et al.* eds., A PATENT SYSTEM FOR THE 21ST CENTURY 31 (2004); James Bessen & Michael Meurer, *Lessons for Patent Policy from Empirical Research on Patent Litigation*, 9 LEWIS & CLARK L. REV. 1 (2005).

[12] Acacia Research Corp., About Us: Corporate Profile, http://www.acaciaresearch.com/aboutus_main.htm (last visited Jan. 23, 2006); *see* Steven M. Cherry, *Company Profile: The Patent Profiteers*, IEEE SPECTRUM, June 2004, at 38-41; *see also* Danny Fortson, *The Big Squeeze*, IP LAW & BUS., Nov. 2004, at 19 (discussing Intellectual Ventures); John Markoff, *Mystery Bidder Obtains Internet Patents*, N.Y. TIMES, Dec. 7, 2004, at C6 (discussing JGR Acquisitions Inc.); Ian Austen & Lisa Guernsey, *A Payday for Patents 'R' Us*, N.Y. TIMES, May 2, 2005, at C1 (noting that the founders of NTP, the plaintiff in the RIM BlackBerry case, designed it as "a kind of virtual company" to "make money from . . . patents").

[13] *See* Kirk L. Kroeker, *Forgent Sues 31 Companies for JPEG Royalties*, TECHNEWSWORLD, Apr. 23, 2004, http://www.technewsworld.com/story/33518.html (discussing Forgent Networks).

at 4. Without products at stake on both sides of the dispute, there is "no leverage to create an incentive for a cross-license or other business resolution." *Id.* But these factors, which might have been taken into account to preclude injunctive relief under traditional balancing of the equities, are of no help to a patent defendant under an automatic injunction rule.

The Federal Circuit's rigid injunction rule, by increasing professional patent litigants' incentive to sue, exacerbates the already serious burden that patent litigation imposes on judicial resources.[14] Although no separate figures detail what portion of the huge increase in patent suits over the last decade is due to professional patent litigants, their simultaneous rise is not mere coincidence.[15] By providing additional incentives to sue, and by making abusive litigation based upon low-value or technically dubious patents economically attractive, the rule deepens this already serious challenge to the administration of justice.

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[14] Between 1994 and 2004, the number of patent suits has increased from 1,600 to over 3,000 – an increase nearly six times the overall increase in civil cases. *See* ADMINISTRATIVE OFFICE OF THE U.S. COURTS, JUDICIAL FACTS AND FIGURES, at Table 2.2 (2005), http://www.uscourts.gov/judicialfactsfigures/alljfftables.pdf. Moreover, when patent cases are litigated, they are more likely than other cases to go to trial. *See, e.g.*, Bessen & Meurer, *supra*, at 3 (noting that patent cases go to trial at twice the overall rate for civil suits). Finally, patent trials tend to be lengthy: almost 10% of patent trials require 20 or more days of trial, compared to less than 1% of all civil cases, and it is not unusual for a patent trial to last for several months. *See, e.g.*, M. Patricia Thayer *et al.*, *Examining Reexamination: Not Yet An Antidote To Litigation*, 5 SEDONA CONF. J. 23, 26 (2004).

[15] *Amici* have experienced a substantial rise in suits by professional patent litigants. Some *amici* estimate that such suits account for two-thirds to three-quarters of their patent dockets.

D. The Automatic Injunction Rule Allows Patent Litigants To Gain Despite Significant Social Costs

The Federal Circuit acknowledges a possible exception to its automatic injunction rule in "exceptional" cases in which there is a "need to use an invention to protect public health." *MercExchange*, 401 F.3d at 1338-39. This exception is so rarely applied, however, as to be effectively meaningless. The Federal Circuit thus, as a practical matter, ignores the public interest that has been a traditional concern of equitable relief. Its rigid rule ensures that in some cases, patent plaintiffs will be able to impose social costs apart from the increased costs that producers will pass along to their customers.

A recent and troubling illustration is provided by a patent infringement case between two competitors in the medical device market. *See Mallinckrodt Inc. v. Masimo Corp.*, No. 00-6506, 2004 U.S. Dist. LEXIS 28518 (C.D. Cal. July 12, 2004). The patents involved in this case related to pulse oximetry, which measures the amount of oxygen being carried in a patient's blood. It is crucial for doctors to know patients' blood oxygen levels, especially for premature babies, those under anesthesia and those suffering respiratory distress. Inadequate blood oxygen can lead to blindness, brain damage and death.

Following a six-week trial in the Central District of California in 2004, a jury determined that Nellcor had willfully infringed four of Masimo's patents and assessed damages of $134 million. *Id.* at *5. On post-trial motions, the district court judge reversed the jury's finding as to one of the patents and reversed the finding of willfulness as to all the patents. *Id.* at *111-*12. The court held a bench trial finding that Masimo had improperly procured one of its patents by intentionally misleading the Patent Office. Significantly, the trial judge denied Masimo's request for injunction, not only because Masimo had unclean hands, but also because doctors

testified that an injunction "would likely compromise patient safety by forcing health professionals to switch back and forth between types of oximeters." *Id.* at *103.

In an unreported opinion, however, the Federal Circuit reversed the district court's denial of the injunction. *Mallinckrodt, Inc. v. Masimo Corp.*, 147 F. App'x 158, 175-78 (Fed. Cir. 2005). It stated that "it is contrary to the laws of property to deny a patentee the right to exclude others from use of his property." *Id.* at 178 (citing the decision below). Such a decision makes clear that the public health exception to the Federal Circuit's automatic injunction rule is so narrow as to be illusory.

Moreover, an exception for public health takes no account of other widespread harms that automatic injunctions can cause to the public. For example, in the BlackBerry case described above, 3.65 million BlackBerry users would be deprived of service if an injunction were enforced against RIM. Hence the Department of Justice raised concerns about the public interest in the Government's robust communication capabilities. *See* Yuki Noguchi, *Government Enters Fray Over BlackBerry Patents*, WASH. POST, Nov. 12, 2005, at D01. Thus the automatic injunction rule can permit patent litigants to inflict vast disruption on established communication networks on which many depend.

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In sum, the Federal Circuit's rule guaranteeing injunctive relief upon a finding of infringement gives patent litigants a weighty club with which to back up shake-down threats that force settlements and license fees disproportionate to the patent's value. It does so both with respect to narrow patent claims over components of complex processes and broad patent claims of dubious technical merit. It encourages the rise of professional patent holding companies that speculate and litigate rather than innovate. And it fails to account for

important aspects of the public interest, including even matters of consumer health and communication. For these very practical reasons, the holding below should be reversed.

II. THE AUTOMATIC INJUNCTION RULE UNDERMINES THE GOALS OF THE PATENT SYSTEM AND DISTORTS PATENT PRACTICE

A. The Automatic Injunction Rule Discourages The Useful Innovation That the Patent System is Intended to Promote

The Constitution empowers Congress to authorize granting patents "[t]o promote the Progress of . . . useful Arts." U.S. CONST. art. I, § 8, cl. 8. As this Court has repeatedly recognized, the goal of patent law is to encourage innovation and bring new designs and technologies into public use. *See, e.g., Aronson v. Quick Point Pencil Co.*, 440 U.S. 257, 262 (1979) (noting that patent law "seeks to foster and reward invention [and] to stimulate further innovation"); *see also Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 401 (1911) ("The purpose of the patent law is to stimulate invention.").

By encouraging abusive litigation in the ways described above, the automatic injunction rule disserves this constitutional purpose. First, by encouraging abusive litigation, the automatic injunction rule saps resources that would otherwise be available for research and innovation. The litigation encouraged by the rule diverts resources that might be more productively used to develop and improve products. Every dollar spent defending against patent suits, especially abusive ones based upon low-value or scientifically dubious patent claims, is a dollar that could be spent more productively on research and development. Moreover, the money spent actually litigating patent cases represents only the tip of the iceberg. Professional patent plaintiffs make most of their

money by simply threatening to bring litigation and thereby extracting disproportionate licensing fees.

Second, the risk of litigation distorts business operations. For smaller firms, the risk of litigation is a major consideration in deciding whether to engage in research and development. Aware that they cannot afford the time and expense of patent litigation, many smaller companies reduce or alter their research and development efforts. *See* JAFFE & LERNER, *supra*, at 15. The research and development decisions of larger companies are affected as well. To avoid patent litigation, these companies often seek defensive patents that they would not otherwise prosecute, thereby reducing the funds available for additional research and development. *See id.* at 58; Ziedonis, *supra*, at 181-83. They also forego pursuing smaller innovations because it is safer to use old components and processes that are clearly in the public domain or for which they already own the patents.

These consequences effectively turn the patent system on its head, undermining its goal of promoting innovation. The automatic injunction rule does not encourage patent holders to exploit their inventions or encourage others to do so to the benefit of the public. To the contrary, it allows patent holders to lie low while others invest time and money in independently discovering their invention, developing it, and incorporating it into a successful product. Then, the patent holder can spring into action to extract a license fee commensurate not with the value of the patent but with the time and money the manufacturer has invested. Far from encouraging innovation, this threat "disrupts the ongoing process of innovation." JAFFE & LERNER, *supra*, at 58.

B. The Automatic Injunction Rule Encourages Counterproductive Practice In The Patent Office

The automatic injunction rule has feedback effects that reverberate back to the application process at the Patent Office. The Federal Circuit's removal of discretion from the courts that ultimately oversee Patent Office activities increases patent applicants' incentives to engage in self-serving practices that can amount to misuse of the system.

The patent process allows applicants to define their own property rights by filing claims of varying scope and to fashion them with enforcement strategy rather than accurate definition of the actual invention in mind. Thus, patent applicants can fashion claims to cover products already in the market or to cover what they perceive to be the direction of the market. Patent applications spawned from earlier inventions can issue and be enforced even while related litigation is pending. A patent owner can sue a defendant, learn about the accused product and defenses, and at the same time, craft patent claims to take the litigation defenses better into account.

The patent application process also does not fix patent rights in time. Patents can issue years after the applications are filed due to Patent Office backlogs and patentee delays. Patent applicants can file continuation applications to extend examinations. *See* 35 U.S.C. § 120; SCHWARTZ, *supra*, at 24-26. In the meantime, other firms might have invested considerable capital in complex plant or network equipment, licensed what they believe to be the rights they need to make and sell their products, and developed their product and service markets. Such practices can be fundamentally unfair to later-alleged infringers, yet ingorance of a patent or patent application is no defense to liability, *see Kewanee Oil*, 416 U.S. at 478 (denying an independent creation defense to patent infringement), and fraud on the Patent Office and

prosecution laches are exceedingly difficult to prove. See *Symbol*, 422 F.3d at 1385

Under traditional equitable principles, however, a court could take account of such sharp patent prosecution practices before issuing an injunction. For example, in determining the irreparability of harm to a plaintiff and balancing the hardships to the parties, a court could take account of when the company charged with infringement learned of the existence of a patent and how much capital it had invested in the technology later patented. It could also distinguish situations where the patentee has understandably extended a patent application while the "art of the pertinent field has become developed," FABER, *supra*, at 3 (noting that "the real 'essence of the invention' is sometimes not fully understood until many years later"), from those where the patentee merely lay in wait to increase its negotiating leverage and capture the benefits of others' technology investments.[16]

In contrast, the automatic injunction rule enables any late-issued patent, regardless of circumstances, to serve as a weighty club. A patent whose issuance is intentionally delayed and whose claims are cleverly drafted to take account of intervening developments (whatever the original invention might have been) can take on an economic leverage disproportionate to its intrinsic technical value.

The Federal Circuit's rule removes the trial courts as a potential check on such abusive practices at the Patent Office. Trial court discretion is especially important in the patent context because of the *ex parte* aspects of the application process. In a land office, the government surveys the

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[16] Equitable principles in a flexible injunction standard could also help curb post-issuance misconduct by patentees that does not rise to the level of unclean hands or patent misuse. *See, e.g.*, *Hynix Semiconductor Inc. v. Rambus, Inc.*, No. 00-20905 (N.D. Cal. filed Jan. 4, 2006) (denying unclean hands defense against patent holding company).

property, and in personal property transfers, the bona fide purchaser for value rule aplies. In the patent context, by contrast, patent holders define their own property rights. When applicants spend more time inventing patents than patenting inventions, they disserve the goal of advancing the "progress of . . . useful Arts." Re-introducing trial court discretion in granting equitable relief would restore a meaningful buffer against such practices and advance the patent system's goal of promoting innovation.

III. THE AUTOMATIC INJUNCTION RULE IS UNNECESSARY BECAUSE OTHER REMEDIES ARE ADEQUATE TO PROTECT INNOVATION

"The federal patent laws have embodied a careful balance between the need to promote innovation and the recognition that imitation and refinement through imitation are both necessary to invention itself and the very lifeblood of a competitive economy." *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 146 (1989). As part of that careful balance, the patent laws include a comprehensive structure for remedying infringement that contains both mandatory and discretionary and both legal and equitable components.

The patent laws provide that "the court *shall* award the claimant damages adequate to compensate for the infringement" of the patent. 35 U.S.C. § 284 (emphasis added). Damages can be no less than "a reasonable royalty." *Id.* A patent holder active in the marketplace can also recover damages in the form of the profits it would have made had the defendant not infringed—*i.e.*, lost sales. *Aro Mfg. Co. v. Convertible Top Replacement Co.*, 377 U.S. 476, 507-08 (1964); *Hebert v. Lisle Corp.*, 99 F.3d 1109, 1119 (Fed. Cir. 1996). Congress included few limitations on the mandatory compensatory damages. *See* 35 U.S.C. §§ 286 (time limita-

tion) & 287 (limitations related to the marking of patented products and notice of infringement).

In contrast to the mandatory nature of compensatory damages, a court has discretion to treble damages and award attorneys' fees in exceptional cases, for example in cases of willful infringement. 35 U.S.C. §§ 284-285. Similarly, the Patent Act calls for discretion with respect to equitable relief, providing that courts "*may* grant injunctions in accordance with the principles of equity to prevent the violation of any right secured by patent, on such terms as the court deems reasonable." 35 U.S.C. § 283 (emphasis added).[17] There is no statutory basis for the Federal Circuit's suggestion that injunctions are mandatory because patents confer exclusive rights; the statute is expressly permissive. Copyright and trademark laws create exclusive rights to intellectual property too, but injunctions in those fields are subject to standard equitable balancing. *See, e.g., Gucci America, Inc. v. Daffy's Inc.*, 354 F.3d 228, 235-39 (3d Cir. 2003); *Abend v. MCA, Inc.*, 863 F.2d 1465, 1479 (9th Cir. 1988).

The Federal Circuit's automatic injunction rule upsets the careful balance Congress created between mandatory and discretionary patent remedies. By eliminating equitable discretion, the rule not only makes mandatory a remedy Congress explicitly intended to be discretionary, but also distorts the monetary rewards received by patent plaintiffs, making

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[17] This Court's decision in *Continental Paper Bag Co. v. Eastern Paper Bag Co.*, 210 U.S. 405 (1908), is not to the contrary. That decision held that the nonuse of a patent does not deprive a court of jurisdiction to grant a patent holder equitable remedies. It did not, however, hold that injunctive relief is automatic regardless of whether a patent owner practices an invention. To the contrary, it expressly reserved the question: "Whether, however, a case cannot arise where, regarding the situation of the parties in view of the public interest, a court of equity might be justified in withholding relief by injunction, we do not decide." *Id.* at 430.

them a far cry from the mandatory compensatory remedy envisaged by Congress.

For example, patent holders who do not practice their patents are entitled to the fair value of the royalties that would have been earned on a license negotiated between the parties, but typically cannot prove damages for lost sales. *See Maxwell v. J. Baker, Inc.*, 86 F.3d 1098, 1108-10 (Fed. Cir. 1996). For a low-value patent, these damages frequently will be minimal and probably not worth the cost of litigation. The Federal Circuit's automatic injunction rule, however, changes the game. The enormous costs imposed by guaranteed injunctive relief create a prospect of lucrative settlements that far exceed the patent's merit, encouraging litigation that otherwise might not take place at all or that would result in far lower damage verdicts.

By contrast, a return to traditional equitable balancing would eliminate many such distortions. As factors that go to irreparable harm, adequacy of legal remedies, public interest, and the balance of hardship, the district courts could consider the burden of an injunction would impose upon a defendant to break up fixed capital investment, the technical value of the patented product or process, the plaintiff's actual practice or licensing of the patent at issue, and the plaintiff's conduct at the Patent Office and after issuance.

For example, a court might well deem injunctive relief unnecessary where a plaintiff does not practice the patent itself nor attempt to exclusively license it to others. In such a case, legal remedies might be sufficient to offset any loss if there is no irreparable or unquantifiable indirect injury to the plaintiff's competitive position.[18] Nor is the prospect of damages illusory. Juries have returned large verdicts for past infringement even to patent plaintiffs who have not invested

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[18] This is not to say that compulsory licensing would ever be appropriate, but only that here, discretionary injunctive relief would not.

capital in manufacturing and development. *See* Chan & Fawcett, *supra*, at 5-6 (noting that the plaintiff in *Eolas Techs., Inc. v. Microsoft Corp.*, 399 F.3d 1325 (Fed. Cir. 2005), obtained damages of $521 million). In addition to compensatory damages for past infringement, the threat of punitive damages and attorneys' fees for willful infringement will deter future infringement after a judgment.

Some patent owners who do not practice their intellectual property might argue that they should not be penalized for failing to have adequate capital to develop and manufacture products. But the automatic injunction windfall does not encourage investment in products. To the contrary, it encourages applicants to obtain as many patents with as broad coverage as possible, whether or not the applicants plan to invest in production or even know if the claimed inventions are possible to practice. Some patent owners might also argue that removing the automatic injunction rule would inhibit efficient secondary markets for patents. The prospect of large compensatory damages and treble damages for willful infringement, however, provide adequate financial reasons for individuals and firms to continue to buy, sell and license patent rights without wasteful investment in patent litigation as a business.

Under a flexible standard, injunctive relief against patent infringement would still remain available where appropriate to prevent irreparable harm to a patent holder. The paradigm example is perhaps where a seller makes unauthorized use of a competitor's patented device. Even where a patent holder does not practice a patent, injunctive relief might sometimes be appropriate—as for example in the case of a for-profit spin-off from a university technology transfer office that initially has only the brainpower of its academic inventors and an exclusive license as its assets. In such a case monetary damages might be insufficient to prevent irreparable harm to the spin-off's potential to produce innovative products.

Courts have long been tasked with weighing such factors when considering injunctive relief, and there is no reason to believe that they cannot return to doing so in patent cases. The prospect of large damages and the possibility of flexible equitable relief, or attorneys' fees and punitive damages for willful infringement provide adequate incentives for individual inventors to seek patent protection.

CONCLUSION

The Federal Circuit's judgment below should be reversed and this Court should instruct the lower courts to return to exercising their traditional equitable discretion when considering injunctions in patent cases as in all other cases arising under federal statutes.

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